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No. 02-1389

In the Supreme Court of the United States

UNITED STATES OF AMERICA, PETITIONER

v.

ABEL COSMO GALLETTI AND SARAH GALLETTI; AND FRANCESCO BRIGUGLIO AND ANGELA BRIGUGLIO

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE UNITED STATES

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QUESTION PRESENTED

Whether, in order to enforce the derivative liability of partners for the tax debts of their partnership, the United States must make a separate assessment of the taxes owed by the partnership against each of the partners directly.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-17a), which superseded the initial opinion of the court (298 F.3d 1107), is reported at 314 F.3d 336.[1] The opinions of the district court (Pet. App. 18a-30a, 31a-43a) are reported at 88 A.F.T.R.2d (RIA) 5580 and 88 A.F.T.R.2d (RIA) 1639. The opinions of the bankruptcy court (Pet. App. 44a-55a, 56a-68a) are reported at 86 A.F.T.R.2d (RIA) 6433 and 86 A.F.T.R.2d (RIA) 6438.

[1] The opinion and judgment of the court of appeals, as well as the order denying the petition for rehearing, contain separate docket numbers for the associated bankruptcy cases of the Gallettis and the Briguglios, who are the general partners of the partnership whose tax liabilities are at issue in this case.

JURISDICTION

The judgment of the court of appeals was entered on August 8, 2002. The petition for rehearing was denied on November 20, 2002. Pet. App. 2a-3a. On February 6, 2003, Justice O'Connor extended the time within which to file a petition for a writ of certiorari to and including March 20, 2003. The petition for a writ of certiorari was filed on that date, and was granted on June 23, 2003. The jurisdiction of this Court rests upon 28 U.S.C. 1254(1).

STATUTORY PROVISIONS INVOLVED

The relevant portions of 11 U.S.C. 101 and 502, 26 U.S.C. 3102, 3111, 3403, 3404, 6201, 6203, 6501 and 6502, and Cal. Corp. Code §§ 16306 and 16307 (West Supp. 2003) are set forth at Pet. App. 69a-73a.

STATEMENT

1. Respondents are the general partners of a partnership named Marina Cabrillo Partners. Pet. App. 4a. During the years relevant to this case, the partnership employed various workers and, as a consequence, accrued liability for federal employment taxes.[2] Federal employment taxes accrue against the "employer" (*e.g.*, 26 U.S.C. 3102(b), 26 U.S.C. 3111(a)) of any person who "performs or performed any service, of whatever nature, as the employee of such person." 26 U.S.C. 3401(d). Because the partnership was the "employer,"

[2] A partnership is not a taxable entity for federal income tax purposes. 26 U.S.C. 701. The Internal Revenue Code instead imposes direct income tax liability on the partners for the income realized by the partnership. 26 U.S.C. 702. As explained in the text, however, the partnership, as the "employer," is itself directly liable for the federal employment taxes associated with its employees. See Pet. App. 62a.

the withheld income taxes, social security (FICA) taxes and Federal Unemployment Tax Act (FUTA) taxes relating to its employees were direct liabilities of the partnership. Pet. App. 62a.

On various dates between 1994 and 1996, the Internal Revenue Service made assessments of the unpaid federal employment tax liabilities of the partnership that accrued for periods from 1992 through the first quarter of 1995. Each of these assessments was made within three years after the filing of the partnership's employment tax return. Pet. App. 4a-5a, 42a. As a consequence of those timely assessments (26 U.S.C. 6501(a)), the federal limitations period for commencing a judicial action to collect the unpaid tax liabilities of the partnership was extended to ten years from the dates of assessment (26 U.S.C. 6502(a)(1)).[3]

2. After respondents encountered financial difficulties, they sought protection from their creditors under Chapter 13 of the Bankruptcy Code. The United States filed proofs of claim in their personal bankruptcy cases to recover the unpaid federal employment taxes owed by the partnership. Pet. App. 45a, 57a.

a. Respondents objected to the proofs of claim. They acknowledged that, as general partners, they were derivatively liable for all lawful debts of the partnership under state law (Cal. Corp. Code § 16306 (West Supp. 2003)). They also acknowledged that the assessments of the employment taxes against the partnership were timely and valid. They contended, however, that

[3] "Until 1990 the statute of limitations for the collection of tax debts was six years from assessment. That year Congress increased the period to ten years. Pub. L. 101-508, amending 26 U.S.C. § 6502(a)." *United States* v. *Wright*, 57 F.3d 561, 562 (7th Cir. 1995).

federal law prohibits the collection of the tax liabilities of the partnership from its partners unless a separate assessment of the taxes has been made against the partners individually. Pet. App. 45a, 58a. They further contended that the United States is now barred by 26 U.S.C. 6501(a) from making such assessments against the partners because more than three years had elapsed since the partnership filed the tax returns for the periods for which the tax liabilities arose. Pet. App. 46a-47a, 59a.

In response, the government explained (i) that the assessments against the partnership were timely and valid and (ii) that the derivative liability of the general partners for the resulting debt of the partnership arises under state law, not under the Internal Revenue Code. Accordingly, when, as here, a valid assessment has been made of the tax liability of the *partnership*, no additional, individual assessment against the partners is required by federal law to permit suit to proceed against the partners for their derivative, state-law liability. Pet. App. 47a, 59a.

b. The bankruptcy court disallowed the government's claims, and the district court affirmed that ruling. Relying on the proposition that "a valid assessment is a prerequisite to tax collection" (Pet. App. 28a (quoting *El Paso Refining, Inc.* v. *IRS*, 205 B.R. 497, 499 (Bankr. W.D. Tex. 1996)), these courts held that the employment taxes owed by the partnership must be assessed against the partners directly before they could be collected directly from them. Because no assessment had been made against the partners individually within the three-year period provided by 26 U.S.C. 6501, the bankruptcy court and district court concluded that the government's claims are now barred in this case. Pet. App. 28a-29a, 41a-42a; *id.* at 51a-54a, 62a-66a.

3. The court of appeals affirmed. Pet. App. 1a-17a. The court first stated that, under Section 6501(a) of the Internal Revenue Code, the government is to collect tax deficiencies "by making an assessment against the taxpayer within three years of the filing of the taxpayer's return." Pet. App. 6a. The court reasoned that respondents, as general partners, are "taxpayers" who are subject to assessment for the employment taxes owed by the partnership. The court noted that the term "taxpayer" is defined in Section 7701(a)(14) of the Code as "any person subject to any internal revenue tax" and Section 7701(a)(1), in turn, defines the word "person" to include "an individual" as well as a "partnership." Pet. App. 7a-8a. Relying on these definitional provisions, the court concluded that, while "[t]he Partnership is a 'taxpayer' within the meaning of the statute, * * * so also is each individual [partner] a separate 'taxpayer'" subject to assessment for this tax. Pet. App. 8a.

The court next concluded that the timely assessments against the partnership in this case "extended the statute of limitations only with respect to the Partnership" and "left unaltered the limitations period applicable to [respondents]." Pet. App. 8a. Because the government did not "assess" the partnership's tax liabilities against the partners individually within three years after the partnership returns were filed, the court held that the government is now barred by Section 6501(a) from collecting those taxes from respondents. *Ibid.*

The court of appeals rejected the government's argument that assessments against the individual partners are unnecessary in this action brought to enforce the derivative, state-law liability of the partners for the valid debts of the partnership. The court acknowledged

that, "under California law, partners are 'personally liable for the debts and liabilities of the partnership, including its tax liability.'" Pet. App. 14a (quoting *Young* v. *Riddell*, 283 F.2d 909, 910 (9th Cir. 1960)). Even though "under state law each individual partner is *liable* for the debts of the partnership," the court stated that "a creditor may collect a debt for which the partner is jointly and severally liable only by first obtaining a judgment against the partner." Pet. App. 16a. The court concluded that, since "[t]he IRS has obtained no judgment against [respondents,]" and since "[t]he time for doing so has expired," the partners may not now be held liable for the tax debts of the partnership. *Ibid.*

4. In a petition for rehearing with suggestion for rehearing en banc, the government argued that the panel decision in this case conflicts with the decision of the Seventh Circuit in *United States* v. *Wright*, 57 F.3d 561 (1995). In response to the petition for rehearing, the court amended its opinion to state that "*Wright* is distinguishable because, in that case, the IRS had assessed both the partnership * * * and the individual partners." Pet. App. 2a. The court acknowledged that the action by the government to collect taxes owed by the partnership from the individual partners in *Wright* was brought *after* the end of the limitations period that would have been applicable if the individual partners had been directly liable for the tax under federal law. Pet. App. 3a. The court nonetheless stated that, because both the partners and the partnership received assessments in *Wright*, "[t]he Seventh Circuit * * * had no opportunity to address the question before us." *Ibid.*

SUMMARY OF ARGUMENT

The United States made a timely assessment of federal employment tax obligations owed by a partnership. When the partnership failed to pay, the United States sought to enforce these tax liabilities against respondents who, as general partners, were derivatively liable under state law for all valid debts of the partnership. The court of appeals erred in concluding that the United States could not enforce its derivative claim against the partners without first "assessing" the tax against each of the partners individually.

1. The taxes involved in this case accrued from the operations of a partnership. As a matter of federal law, the partnership itself was directly liable for those taxes. The derivative liability of the partners for the taxes owed by their partnership arose under state law, not under the provisions of the Internal Revenue Code. Under the applicable principles of state partnership law, it is well established that partners are derivatively liable "for the debts and liabilities of the partnership, including its tax liabilities." *Young* v. *Riddell*, 283 F.2d 909, 910 (9th Cir. 1960).

The taxes owed by the partnership were validly assessed under the applicable provisions of federal law, and the existence of a valid partnership debt is therefore not disputed in this case. It is also undisputed that, under state law, the partners are derivatively liable for the valid debts of the partnership. The courts below therefore erred in refusing to enforce the government's claim in this case.

2. The Internal Revenue Code does not require that separate assessments be made for each partner in order to enforce their derivative liability for partnership

taxes under state law. Section 6201(a) of the Code authorizes assessment of "all taxes * * * imposed by this title." 26 U.S.C. 6201(a). The assessment of a tax is a formal bookkeeping notation by which the amount of a tax liability is officially recorded. As the predecessor of the Federal Circuit explained in *Anderson* v. *United States*, 15 F. Supp. 216, 225 (Ct. Cl. 1936), cert. denied, 300 U.S. 675 (1937), it is the "tax" and not the "taxpayer" that is assessed. Once the amount of the "tax" is assessed, no additional or separate "assessment" is required to collect the tax, either from the party who is directly liable for the tax or from other parties who are derivatively liable for it. *Ibid.*

When the amount of the tax is determined and assessed, the time in which a "proceeding in court" may be commenced to collect that tax is extended to "10 years after the assessment of the tax." 26 U.S.C. 6502(a). This statute of limitations applies equally to proceedings against the taxpayers who are directly liable for a tax and to proceedings against persons, such as respondents, whose liability is only derivative. Because the current "proceeding in court" to collect the assessed taxes was "begun * * * within 10 years after the assessment of the tax" (*ibid.*), it is therefore timely as a matter of federal law.

As numerous decisions of this Court and of the other courts of appeals have concluded in a variety of settings, once the tax owed by the directly liable taxpayer has been assessed, no additional or further assessment need be directed to a party whose liability for a tax is only derivative. The court below erred in failing to respect and follow that precedent in this case.

3. The court of appeals also erred in suggesting that California partnership law precludes collection of the tax debts involved in this case. Section 16307(c) of the

California Corporations Code, on which the court relied, specifies that "a judgment against a partnership may not be satisfied from a partner's assets unless there is also a judgment against the partner." Pet. App. 73a.

Claims are allowable in bankruptcy court, as a matter of federal law, "whether or not" a preexisting judgment has been obtained against the debtor. 11 U.S.C. 101(5)(A). Moreover, bankruptcy court proceedings on disputed claims result in a judgment of that court that is binding on the parties and has res judicata effect. Since, on the merits, the amount and validity of the tax debt are not disputed in this case, any requirement that a judgment be obtained prior to collection of the partnership debt from the partners would be satisfied on remand upon the allowance of the government's meritorious claim.

ARGUMENT

THE UNITED STATES MAY ENFORCE THE DERIVATIVE LIABILITY OF PARTNERS FOR TAX DEBTS OWED BY THEIR PARTNERSHIP WITHOUT MAKING A SEPARATE ASSESSMENT AGAINST EACH OF THE PARTNERS INDIVIDUALLY

The United States made a timely assessment of federal employment tax obligations owed by a partnership. When the partnership failed to pay, the United States sought to enforce these tax liabilities against the partners, who were derivatively liable under state law for all valid debts of the partnership. The court of appeals erred in concluding that, even though the United States has a valid claim against the partnership for unpaid taxes, the United States may not enforce its derivative state-law claim against the partners without first "assessing" the taxes against the partners individually.

A. The Internal Revenue Code Does Not Require That A Partner Be Assessed Individually For Taxes Owed By The Partnership

1. *The Derivative Liability of Partners for the Tax Debts of a Partnership Arises under State Law, not under the Internal Revenue Code.* The court erred initially by misapprehending the essential nature of the government's claim in this case. The government's derivative claim against the partners for the recovery of taxes owed by the partnership is based upon state partnership law. It is brought under the principles of state law that specify that "all *partners are liable* jointly and severally *for all obligations of the partnership*" (Cal. Corp. Code § 16306(a) (West Supp. 2003) (emphasis added)).[4] While federal law creates the debt of the partnership for these employment taxes (see pages 2-3, *supra*), it is state law that makes the partners derivatively liable for that debt.

Under state partnership principles, it is well established that general partners are "personally liable for the debts and liabilities of the partnership, including its tax liability." *Young* v. *Riddell*, 283 F.2d 909, 910 (9th

[4] This provision is contained in Section 306(a) of the Uniform Partnership Act (1997), which has been adopted by 31 States, the District of Columbia and the Virgin Islands. 6 U.L.A. 117 cmts. 1-2 (2001). California enacted this provision in 1996, 1996 Cal. Stat. ch. 1003 (A.B. 583), § 2, and it was made effective January 1, 1997. As of January 1, 1999, this provision became applicable to "all partnerships," regardless when formed. Cal. Corp. Code § 16111(b). Prior California law had also long provided that general partners are jointly and severally liable for the federal tax debts of their partnership. Cal. Corp. Code § 15103 (repealed); Cal. Corp. Code § 15105 (repealed). *Young* v. *Riddell*, 60-1 U.S. Tax Cas. (CCH) ¶ 9381, at 76,054 (S.D. Cal. 1959), aff'd, 283 F.2d 909 (9th Cir. 1960); see *Danning* v. *United States*, 532 F.2d 725, 726 (9th Cir. 1976); *In re Crockett*, 150 F. Supp. 352, 354 (N.D. Cal. 1957).

Cir. 1960). Accordingly, when (as in this case) a valid "obligation of the partnership" exists under federal law, that lawful debt of *the partnership* may be enforced directly against *the partners* under state law. See *United States* v. *Papandon*, 331 F.3d 52, 55 (2d Cir. 2003) ("state law determines a partner's liability for partnership obligations"); *Remington* v. *United States*, 210 F.3d 281, 283 (5th Cir. 2000) (under state law, "the IRS is entitled to collect the trust fund tax liability, indisputably a partnership debt, from any one of the general partners," because "[t]he partnership is the primary obligor and its partners are jointly and severally liable on its debts"); *Ballard* v. *United States*, 17 F.3d 116, 118 (5th Cir. 1994) ("it is state law that determines when a partner is liable for the obligations—including employment taxes—of his partnership"); *United States* v. *Hays*, 877 F.2d 843, 844 n.3 (10th Cir. 1989) ("the liability of a general partner for the tax obligations of the partnership is determined by state law rather than federal law"); *Calvey* v. *United States*, 448 F.2d 177, 180 (6th Cir. 1971) (same).

In the present case, the uncontroverted record establishes (i) that timely assessments of the partnership's tax liabilities were made within the three-year period allowed by 26 U.S.C. 6501(a), (ii) that those timely assessments extended the time for collection of those tax liabilities for an additional ten-year period (26 U.S.C. 6502(a)), and (iii) that this ten-year period has not yet expired. See Pet. App. 16a. The existence of the partnership debt, and the liability of the partners for that debt under state law, are thus both undisputed in this case. See *ibid.* See also *Tony Thornton Auction Services, Inc.* v. *United States*, 791 F.2d 635, 638 (8th Cir. 1986) ("the individual partners" are "jointly and

severally liable for the taxes validly assessed against the partnership").

2. *No Assessment of Partners is Required to Permit Collection of Their Derivative Liability for Taxes Owed by the Partnership.* Without directly challenging the established rule that general partners are liable for the valid debts of their partnership under state law, the court of appeals concluded that these taxes could not be collected from the partners in this case because they had been assessed by the IRS only against the partnership and not directly against the partners. Pet. App. 7a-8a. The court stated that, because no assessment was made against the partners "within the three-year period provided under §6501(a), [that statute] bars [the government] from collecting the unpaid debts of the Partnership directly from [the partners]." Pet. App. 8a.[5] This conclusion of the court of appeals is based on

[5] The period of limitations for the United States to enforce a claim held "in its governmental capacity" is determined by federal, rather than state, law. *United States* v. *Summerlin*, 310 U.S. 414, 417 (1940). See *United States* v. *John Hancock Mut. Life Ins. Co.*, 364 U.S. 301, 308 (1960)("the United States is not subject to local statutes of limitation"). In *United States* v. *California*, 507 U.S. 746, 757 (1993), this Court stated that the cases applying this rule to state-law causes of action have involved situations in which "either the right at issue was obtained by the Government through, or created by, a federal statute" or "a federal statute provided the statute of limitations." In the present case, (i) the government plainly proceeds in its sovereign capacity in seeking to collect unpaid federal tax obligations; (ii) those underlying obligations are "created by" federal statute; and (iii) 26 U.S.C. 6502 provides the period of limitation for the collection of taxes either from persons directly or derivatively liable for them. See *United States* v. *Updike*, 281 U.S. 489, 494 (1930) ("[t]he aim in the one case, as in the other, is to enforce a tax liability"). Respondents acknowledge that Section 6501 and Section 6502 govern this case.

a fundamental misunderstanding of the function and nature of an assessment under the Internal Revenue Code.

a. The Internal Revenue Code does not require that separate assessments be made for each partner in order to enforce their derivative liability for partnership taxes under state law. An assessment is merely a formal record of the amount of tax that is due. Once the amount of a tax is determined and recorded in an assessment, the Commissioner may enforce that liability against *any* party that is directly or derivatively liable for it.

Section 6201(a) of the Internal Revenue Code authorizes the Secretary of the Treasury "to make * * * assessments of all taxes * * * imposed by this title." 26 U.S.C. 6201(a). An assessment is made "by recording the liability of the taxpayer in the office of the Secretary [of the Treasury] in accordance with rules or regulations prescribed by the Secretary." 26 U.S.C. 6203. Section 301.6203-1 of the Treasury Regulations states that an assessment is made by the "assessment officer signing the summary record of assessment" which, "through supporting records," provides "identification of the taxpayer, the character of the liability assessed, the taxable period, if applicable, and the amount of the assessment." 26 C.F.R. 301.6203-1.[6] The

They contend, for the reasons adopted by the courts below, that the time provided by these governing federal statutes has expired.

[6] The "summary record of assessment" described in this regulation has historically been made on Form 23C and, more recently, on a similar computer-generated form entitled RACS Report 006. See *March* v. *IRS*, 335 F.3d 1186, 1188 (10th Cir. 2003); *Huff* v. *United States*, 10 F.3d 1440, 1446 & n.5 (9th Cir. 1993). Each "summary record of assessment" aggregates *all* of the taxes, penalties and interest assessed for income, excise, estate, gift and employ-

assessment of a tax is thus "essentially a bookkeeping notation" that serves as a formal record of the amount of the tax liability. *Laing* v. *United States*, 423 U.S. 161, 170 n.13 (1976); *United States* v. *Dixieline Financial, Inc.*, 594 F.2d 1311, 1312 (9th Cir. 1979). And, "through supporting records" that are not part of the assessment document itself, the name and address of the taxpayer who is directly liable for the taxes is also identified. 26 C.F.R. 301.6203-1.

As the predecessor of the Federal Circuit explained in its early decision in *Anderson* v. *United States*, 15 F. Supp. 216, 225 (Ct. Cl. 1936) (emphasis added), cert. denied, 300 U.S. 675 (1937):

> *The assessment contemplated by and referred to in the statute is the assessment by the Commissioner of the tax and the Commissioner's assessment list, which the Commissioner actually signs when he makes an assessment of the tax, does not contain the names of any taxpayers but contains only the amounts and the total tax* as "additional assessments made by the Commissioner." * * * Attached to this assessment list of the Commissioner are separate sheets for use by the collector in keeping his record of collections, credits, and balances due on which is written the name of the person or corporation in respect of whose taxes the amount stated on the Commissioner's assessment list has been assessed.

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ment taxes at a particular service center on a particular date. The "summary record of assessment" does not identify any particular taxpayer or any particular tax period. Any identifying information is set forth in the "supporting records" that are not part of the assessment document itself. 26 C.F.R. 301.6203-1.

The designation on supplementary sheets "of the person in respect of whose income a tax was assessed or the person from whom collection should be made is for the information and guidance of the collector." 15 F. Supp. at 228. The Commissioner's practice in this regard has remained consistent in the ensuing decades since *Anderson* was decided. See note 6, *supra*.

In the present case, it is undisputed that a timely assessment of the taxes owed by the partnership was made. Pet. App. 5a. No other or further "assessment" of these taxes is contemplated, or required, by this statute.

b. When (as in the present case) the IRS makes a timely assessment of a tax, two important consequences ensue.[7] First, after a tax is assessed, the IRS may employ administrative enforcement methods such as tax liens and levies to collect the outstanding tax. 26 U.S.C. 6321-6327, 6331-6344.[8] Second, when a timely

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[7] Even without any assessment of a tax, the United States may bring suit against any party liable for the tax to reduce the unassessed liability to judgment. Section 6501(a) of the Code makes this clear by specifying that "no proceeding in court *without assessment*" for the collection of any tax "shall be begun after the expiration of" three years from the date the applicable tax return was filed. 26 U.S.C. 6501(a). Under this statute, a collection suit may be begun either with or "without assessment" prior to the expiration of this three-year period. *Goldston* v. *United States*, 104 F.3d 1198, 1201 (10th Cir. 1997) (even in "the absence of an assessment" the government "may still file a civil action" or "a proof of claim in a bankruptcy proceeding" to collect the tax during this initial three-year period).

[8] The federal tax lien arises only "at the time the assessment is made." 26 U.S.C. 6322. In addition, before a tax lien arises or seizure and sale of property by levy may occur, the Secretary is to give notice of the assessment to, and make demand for payment upon, "each person liable for the unpaid tax" within 60 days after

assessment is made, the time within which the IRS may collect the tax either administratively *or* by a "proceeding in court" is extended to 10 years after the date of assessment. 26 U.S.C. 6502(a).

In the present case, the IRS properly made a timely assessment of the taxes owed by the partnership. The federal taxes at issue in this case are imposed directly on the "employer." 26 U.S.C. 3102(b) ("[e]very employer" required by 26 U.S.C. 3102(a) to deduct the employees' share of FICA taxes imposed by 26 U.S.C. 3101 "shall be liable for the payment of such tax"); 26 U.S.C. 3111(a) (the employer's share of FICA taxes is imposed on "every employer * * * with respect to having individuals in his employ"); 26 U.S.C. 3301 (same re FUTA taxes); 26 U.S.C. 3403 ("the employer" is liable for the income taxes withheld from employees' wages). When the partnership paid wages to its employees, it thereby created employment tax liabilities for itself, as the "employer," under federal law. See *Otte* v. *United States*, 419 U.S. 43, 51 (1974); *In re Armadillo Corp.*, 410 F. Supp. 407, 410 (D. Colo. 1976), aff'd, 561 F.2d 1382 (10th Cir. 1977).[9]

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making the assessment. 26 U.S.C. 6303(a), 6321, 6331(a). Notice and demand for payment are not, however, preconditions to the filing of a judicial collection suit. *United States* v. *Chila*, 871 F.2d 1015, 1018-1019 (11th Cir. 1989); *United States* v. *Berman*, 825 F.2d 1053, 1060 (6th Cir. 1987); *United States* v. *Hunter Eng'rs & Constructors, Inc.*, 789 F.2d 1436, 1441 (9th Cir. 1986), cert. denied, 479 U.S. 1063 (1987). Nor, as the plain text of the statute makes clear, is such notice and demand a condition for the extension of the period of limitations for such a suit under Section 6502(a), 26 U.S.C. 6502(a). See *Blackston* v. *United States*, 778 F. Supp. 244, 248 (D. Md. 1991).

[9] For purposes of income tax withholding, the term "employer" is generally defined as "the person for whom an individual performs or performed any service, of whatever nature, as the employee of such person." 26 U.S.C. 3401(d). The cited cases applied the same definition for purposes of FICA and FUTA taxes under 26 U.S.C. 3102, 3111, and 3301.

The government made a timely assessment of those taxes within the three-year period allowed by Section 6501(a) of the Internal Revenue Code, 26 U.S.C. 6501(a). Pet. App. 5a. And, under Section 6502(a), that timely assessment of the tax extended for ten years the period in which a judicial action could be commenced to collect that liability (26 U.S.C. 6502(a)):

> Where the assessment of any tax imposed by this title has been made within the period of limitation properly applicable thereto, such tax may be collected by levy or by a proceeding in court * * * begun * * * within 10 years after the assessment of the tax.

This extension of the collection period applies without regard to the identity of the party against whom the action is commenced. It applies equally to a proceeding against a taxpayer who is directly liable for a tax and to a proceeding against a person who is derivatively liable for it. Because the current "proceeding in court" to collect the assessed taxes was "begun * * * within 10 years after the assessment of the tax" (*ibid.*), it is timely as a matter of federal law under these provisions.

c. The court of appeals incorrectly rejected this straightforward application of these statutes on the ground that they apply only when the assessment is made "against the taxpayer" from whom the taxes are being collected. Pet. App. 6a. The court failed to understand that, when a valid assessment is made of the tax owed by the person directly or primarily liable,

no further or separate assessment is required before a collection action may proceed against individuals who are derivatively liable for the tax.

The Code's text itself reveals the error of the court of appeals' interpretation. Section 6501(a) provides that "*the amount of any tax* imposed by this title *shall be assessed* within 3 years after the return was filed," 26 U.S.C. 6501(a) (emphasis added), thus making clear that it is the *amount of the tax*, not the taxpayer or person derivatively liable, that must be assessed. Similarly, Section 6502(a) provides that, "[w]here *the assessment of any tax*" has been timely made, suit may be brought to collect "such tax" "within 10 years after *the assessment of the tax*." 26 U.S.C. 6502(a) (emphases added). This statutory language confirms that Congress contemplated a single "assessment of any tax," and that such assessment would trigger the 10-year period of Section 6502(a)(1) without regard to the identity of the person or persons ultimately found liable to pay the tax. Nothing in the text of these provisions provides any support for the court of appeals' contrary view that "individual assessments" against each potentially liable person are required before Section 6502(a)(1) becomes applicable.

This reading of the statutory text is confirmed by a long-established body of case law holding in a variety of contexts that tax collection actions may proceed against derivatively liable persons in the absence of a separate, individual assessment naming those persons. In *Leighton* v. *United States*, 289 U.S. 506 (1933), for example, this Court addressed an analogous issue involving the derivative liability of transferees of corporate assets for taxes owed by the corporation. The Court expressly rejected the transferees' argument that the statute "require[d] an assessment against them" as a

prerequisite to the collection action. *Id.* at 509. Instead, the Court held that the right of the United States to enforce this derivative liability is based on the assessment against the primarily liable corporation and exists even "without assessment" of the tax against the parties whose liability was only derivative. *Id.* at 508-509. In *United States* v. *Updike*, 281 U.S. 489, 494 (1930), the Court similarly concluded that, because the tax imposed on the corporation "is the basis of the liability" of the transferee, the same limitations period that applies in a suit to collect from the directly liable corporation also applies in a suit against the derivatively liable transferee.

The Seventh Circuit relied upon this Court's decision in *Updike* in *United States* v. *Wright*, 57 F.3d 561 (1995). In *Wright*, as in the present case, the court addressed the statute of limitations that governs an action to collect a partner's derivative state-law liability for unpaid federal employment taxes incurred by a partnership. The question in that case, as in the present one, was "whether, if a suit against the taxpayer would be timely, then suit is also timely against persons derivatively liable." 57 F.3d at 564.[10] The Seventh

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[10] The court below erred in this case in stating that "*Wright* is distinguishable because * * * the IRS had assessed both the partnership * * * and the individual partners." Pet. App. 13a (emphasis omitted). The government had maintained in *Wright* that "the assessments were levied against the partnership only and not against any of the partners individually." *United States* v. *Wright*, 868 F. Supp. 1070, 1071 n.1 (S.D. Ind. 1994). The district court in *Wright* "made clear" that, although it appeared that an assessment may have been entered against the partners as well as against the partnership, that question was "not material to the resolution" of the case. *Ibid.* The Seventh Circuit also did not suggest that the existence of assessments against the partners would have been relevant in *Wright*. See 57 F.3d at 562-563. To

Circuit explained in *Wright* that, under the reasoning of this Court in *Updike*, "the governing principle is all-for-one, one-for-all." 57 F.3d at 563. The court concluded that (*id.* at 564):

> suits against persons derivatively liable for taxes are timely, or not, according to the rules for timeliness of suits against taxpayers. It is hard to escape that conclusion, for both [26 U.S.C.] § 6502 and § 6503 establish rules for suing taxpayers; they do not set up separate periods for persons secondarily liable. Their structure presumes that there is only one period per tax *debt*, no matter how many different persons may be liable on the debt.

Prior to the decision in this case, this rule had long been followed in the lower courts. For example, more than 65 years ago, the predecessor of the Federal Circuit explained that it is incorrect to assume, as the court of appeals did here (Pet. App. 6a-8a), "that the Commissioner of Internal Revenue assesses the taxpayer instead of assessing the tax." *Anderson* v. *United States*, 15 F. Supp. 216, 225 (Ct. Cl. 1936).[11] Because it is the "tax," and not the "taxpayer," that is assessed, the court in *Anderson* held that a separate assessment is not required to collect a tax from a party who is derivatively liable for it. *Ibid.* (estate executor derivatively liable without assessment for taxes owed by decedent). See also page 14, *supra*. As the court

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the contrary, in a holding that directly conflicts with the decision in this case, the court concluded that "suits against persons derivatively liable for taxes are timely, or not, according to the rules for timeliness of suits against taxpayers." *Id.* at 564.

[11] As the predecessor of the Federal Circuit, the decisions of the Court of Claims are binding precedent in that circuit. *South Corp.* v. *United States*, 690 F.2d 13678, 1370 (Fed. Cir. 1982).

explained in a companion case in *Anderson*, so long as the assessment of the "tax" was timely, "the Commissioner had six [now ten] years thereafter within which to make collection" from any person who may be liable for it. *Id.* at 229.

Numerous other courts have adopted and applied this same basic rule in various contexts. As these courts have recognized, a "[f]urther independent assessment [against the party derivatively liable for the tax] would accomplish nothing." *United States* v. *Dixieline Financial, Inc.*, 594 F.2d 1311, 1312 (9th Cir. 1979). See also *United States* v. *Walker*, 217 F. Supp. 888, 890 (W.D.S.C. 1963) (for a collection action to proceed against a derivatively liable party, "[t]he Commissioner is required to assess the tax * * * rather than assess the taxpayer."). For example, in *Payne* v. *United States*, 247 F.2d 481, 484, 489 (8th Cir. 1957), cert. denied, 355 U.S. 923 (1958), the court held that the limitations period under Section 6502(a) for a suit claiming derivative liability of a transferee extended for six [now ten] years after assessment of the tax even though "no assessment * * * had ever been made" against the transferee.

The Tenth Circuit recently reached this same conclusion in *United States* v. *Botefuhr*, 309 F.3d 1263 (2002). In that case, the government sought to collect a gift tax from the donee, who was derivatively liable for the tax only "to the extent of the value of such gift" (26 U.S.C. 6324(b)).[12] The court rejected the argument of the donee that he was relieved of liability because an

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[12] The Internal Revenue Code imposes primary liability for the federal gift tax upon the donor. 26 U.S.C. 2502(c). If the donor fails to pay the tax, however, the donee is personally liable for the tax to the extent of the value of the gift. 26 U.S.C. 6324(b).

assessment had not been made directly against him. The court explained that a timely "assessment" of the *tax* owed by the donor (who was primarily liable) had been made and that, since "the suit would be timely brought against the donor under these provisions, it will be considered timely against the donee or transferee" even though no separate assessment had been made against him. 309 F.3d at 1277-1278. "[B]ecause the IRS is acting within the time period in which it could act against the donor," the court said, "its case against [the derivatively liable] donee is timely." *Id.* at 1278.

d. Accordingly, prior to the decision in this case, the decisions of this Court and other courts of appeals had consistently held that an assessment of a party whose liability for a tax is only derivative is not required to extend the statute of limitations provided by Section 6502(a). Under the holdings of these numerous, consistent decisions, the government's collection action in the present case is timely because it was brought "within 10 years after the assessment of the tax" owed by the partnership. 26 U.S.C. 6502(a)(1). The court below erred by failing to honor and follow this substantial body of precedent in this case.

The erroneous conclusion of the Ninth Circuit in this case is also refuted by other decisions of that same circuit. For example, the Ninth Circuit has held in analogous situations that, when the IRS makes a timely assessment of employment taxes against an employer, that assessment is sufficient by itself to extend the time for bringing suit to recover the derivative liability of a lender under Section 3505 of the Code. The lender's derivative liability for employment taxes closely parallels the derivative liability of a partner under state law. Under Section 3505(a), a lender that pays wages directly to the employees of another employer is liable itself for the amount of taxes required to be deducted and withheld from the wages. 26 U.S.C. 3505(a). Under Section 3505(b), a lender is also liable if it supplies funds to an employer for the specific purpose of paying wages "with actual notice or knowledge * * * that such employer does not intend to or will not be able to make timely payment" of the requisite withholding taxes. 26 U.S.C. 3505(b). The lender's liability, like the partner's liability for partnership employment taxes, is derivative because it arises when the employer fails to pay the taxes imposed. In decisions that were not explained or even discussed by the panel in this case, the Ninth Circuit held that an assessment of liability against the employer is sufficient to extend the limitations period for filing suit against the lender on its derivative liability for that tax. *United States* v. *Dixieline Financial, Inc.*, 594 F.2d 1311 (9th Cir. 1979). The court stated that "the assessment of the tax against * * * the employer * * * met the requirements of § 6501(a)" and that "[f]urther independent assessment" against the derivatively liable lender was unnecessary and "would accomplish nothing." 594 F.2d at 1312-1313.[13] Accord, *United States* v. *First Nat'l Bank of Circle*, 652 F.2d 882, 889 (9th Cir. 1981).

In upholding that same conclusion in *United States* v. *Hunter Engineers & Constructors, Inc.*, 789 F.2d 1436, 1441 (1986), cert. denied, 479 U.S. 1063 (1987), the Ninth Circuit noted that a shorter limitations period for

[13] In fact, in *Jersey Shore State Bank* v. *United States*, 479 U.S. 442, 447 (1987), the Court observed that a lender's liability under Section 3505 cannot be assessed: "[T]he legislative history of § 3505 makes clear that the Government may forcibly collect against a lender only by filing a civil suit."

the derivatively liable lenders than for the employers would be unwise, for it would force the government to file an action against the lenders within three years after the return was filed even if collection efforts against the employer remained ongoing. *Ibid.* The court emphasized that the parties whose liability was only derivative "would suffer if the government was forced to look to them for collection sooner than against employers." *Ibid.*[14]

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[14] The court below also erred in suggesting that one of its own "precedents weigh against the IRS's position" in this case. Pet. App. 8a-11a. The case on which the court erroneously relied was *Young* v. *Riddell*, 283 F.2d 909 (9th Cir. 1960), aff'g 60-1 U.S. Tax Cas. (CCH) ¶ 9381 (S.D. Cal. 1959). In that case, the district court stated that, "[w]here taxes are assessed against a partnership and under state law each member of the partnership is jointly and severally liable for the debts of the partnership, *it is unnecessary and superfluous to name the individual partners in the assessment in order to create liability*; their liability arises as a matter of state law." 60-1 U.S. Tax Cas. (CCH) at 76,054 (emphasis added). The Ninth Circuit affirmed that decision, noting that the individual partner was "personally liable for the debts and liabilities of the partnership, including its tax liability" and would remain so "until the taxes were paid or otherwise discharged as to [the partner]." 283 F.2d at 910-911. This holding in *Young* is plainly consistent with the established rule that taxes may be collected from parties who are derivatively liable without need for separate and additional assessments issued to them directly.

The court of appeals similarly erred in seeking to rely (Pet. App. 11a-12a) on what it acknowledged was "dictum" in *United States* v. *Coson*, 286 F.2d 453 (9th Cir. 1961). As the court explained in *Marvel* v. *United States*, 719 F.2d 1507, 1514 (10th Cir. 1983), "*Coson* deal[s] with the question of whether a federal tax lien was properly perfected. [It does] not stand for the principle that an inadequate notice [of assessment and demand for payment under 26 U.S.C. 6323] bars the Government from obtaining a judgment for tax liabilities due and owing by taxpayers, whether or not named in the notice and demand for payment."

B. California Partnership Law Does Not Preclude Collection Of The Partnership Tax Debts Involved In This Case

The court of appeals acknowledged that, "under California law, partners are 'personally liable for the debts and liabilities of the partnership, including its tax liability.'" Pet. App. 14a (citing *Young* v. *Riddell*, 283 F.2d at 909). The court stated, however, that state law permits "a creditor [to] collect a debt for which the partner is jointly and severally liable only by first obtaining a judgment against the partner." Pet. App. 16a (citing Cal. Corp. Code § 16307(c)). The court concluded that, since "[t]he IRS has obtained no judgment against [respondents,]" and since "[t]he time for doing so has expired," the partners may not now be held liable for the tax debts of the partnership. *Ibid.*[15]

The court erred in concluding that state partnership law bars the recovery sought in this case. Section 16307(c) of the California Corporations Code, on which the court relied, specifies that "[a] judgment against a partnership may not be satisfied from a partner's assets unless there is also a judgment against the partner." Pet. App. 73a. Nothing in that statute addresses or purports to govern the question of federal tax administration presented in this case.

As the decisions of the Federal Circuit, Seventh Circuit, Eighth Circuit and Tenth Circuit described above all make clear, the timely assessment of an

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[15] Although the court presented this conclusion as a distinct alternative to its holding that the timely assessment of the partnership's employment tax liability did not extend the time for collection of that liability directly from the partners under 26 U.S.C. 6501(a), the court's state-law analysis plainly rests on that same reasoning. See Pet. App. 6a, 14a-17a.

employment tax liability permits an action to collect that tax against any primarily or derivatively liable party "by a proceeding in court * * * begun * * * within 10 years after the assessment of the tax." 26 U.S.C. 6502(a)(1). Because the government's tax collection action in these bankruptcy proceedings was commenced "within 10 years after the assessment of the tax" (*ibid.*), it is timely.

We do not dispute that, if the government brought suit against the partnership to recover its unpaid taxes, a judgment solely against the partnership would not permit the IRS immediately to look to the partners' assets for collection of the judgment under Cal. Corp. Code § 16307(c). This case, however, is obviously different. This case was brought by the United States in bankruptcy court to enforce the derivative liability of the individual partners for the tax debt of their partnership. Because respondents had filed for bankruptcy, the United States was barred by the automatic stay from bringing suit outside of bankruptcy court to enforce this derivative liability. 11 U.S.C. 362(a)(1). When the government asserted its claims in the bankruptcy proceedings (11 U.S.C. 501(a)), respondents exercised their right to object to the allowance of the claims (11 U.S.C. 502(a)). After such objections were filed, the bankruptcy court was to determine the validity and amount of the government's claim "after notice and a hearing." 11 U.S.C. 502(b).[16] The adjudication and determination of a disputed claim in the bank-

[16] The Bankruptcy Code does not require a preexisting judgment as a prerequisite for allowance of a claim in bankruptcy. Instead, it requires only a "right to payment, *whether or not such right is reduced to judgment*, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured." 11 U.S.C. 101(5)(A) (emphasis added).

ruptcy case results in a judgment that has res judicata effect. *Katchen* v. *Landy*, 382 U.S. 323, 334 (1966) (citing cases).

Such bankruptcy court proceedings on a disputed claim obviously comport with any requirement that there be a "judgment against a partner" before the liability of a partnership may be collected "from a partner's assets" (Cal. Corp. Code § 16307(c)). The order allowing a disputed claim in bankruptcy court is a judgment with res judicata effect that is enforceable against the debtors and their property. Since, on the merits, the amount and validity of the tax debt are not disputed in this case, any requirement that a judgment be obtained prior to collection of the partnership debt from the partners would thus be satisfied on remand upon the allowance of the government's meritorious claim. In any event, such a claim is allowable in bankruptcy court as a matter of federal law "whether or not" a preexisting judgment had been obtained. 11 U.S.C. 101(5)(A). See note 16, *supra*.

C. The Decision Of The Court Of Appeals Would Impede And Burden Routine Enforcement Of The Tax Laws

The decision of the court of appeals would create severe and impracticable burdens for routine enforcement of the tax laws. We are advised by the Internal Revenue Service that there are currently outstanding partnership employment tax liabilities in excess of $10 billion that have been timely assessed but for which separate assessments have not been made against partners individually. The decision of the court of appeals would routinely bar collection of those liabilities from individual partners in cases in which the ordinary three-year period for assessment of taxes in 26 U.S.C. 6501(a) has expired.

It is undisputed that general partners are jointly and severally liable for all outstanding debts of the partnership under applicable principles of state law. See note 4, *supra*. Until now the IRS has typically pursued collection of partnership tax obligations from the partnerships before commencing litigation with partners to satisfy outstanding tax obligations. Under the abbreviated limitations period that would result from the decision in this case, however, the government would be forced to bring collection suits against partners within the three-year period prescribed in Section 6501(a), even though parallel efforts against the partnership may remain ongoing. A requirement that such duplicative proceedings be pursued would be burdensome for partners as well as for the government, because it would subject partners to the necessity of litigation over matters that the partnership itself should routinely resolve. As the Ninth Circuit pointed out in a related context in *United States* v. *Hunter Engineers & Constructors, Inc.*, 789 F.2d at 1441, persons whose liability for taxes is only derivative "would suffer" severely if the government were forced to pursue such premature and duplicative collection actions. In short, the "doctrine [for which respondents contend] would be attended in practice with great inconvenience, and would seldom lead to any good. Fortunately, the law is not so unreasonable." *The Nitro-glycerine Case*, 82 U.S. (15 Wall.) 524, 535 (1872).

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted.

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